

CHAPTER 1**INTRODUCTION AND SUMMARY****★0101 GENERAL**

Under the provisions of 31 U.S.C. 3515, beginning with fiscal year (FY) 1996, the Department is required to have audited financial statements covering all accounts and associated activities of the Department. As implemented by the Office of Management and Budget (OMB), the Department is required to prepare both Agency-wide financial statements and separate audited financial statements for several individual reporting entities, e.g., Army, Navy, and the Air Force general funds (GF) and working capital funds (WCF). Those financial statements are expected to provide information to the Department of Defense (DoD) program managers, the Congress, and the public, thereby facilitating both effective allocation of resources and assessment of management performance and stewardship. The objective is to produce statements that are accurate, consistent, and meaningful--statements that can and will be used to improve the management of the Department. Additionally, consistent with the objectives of the Statements of Federal Financial Accounting Concepts (SFFACs) and Statements of Federal Financial Accounting Standards (SFFASs), the Department continues to work toward the integration of budget and financial information in order to provide for more effective program management at all levels.

★0102 BACKGROUND

Federal agencies traditionally prepared financial reports to monitor and control the obligation and expenditure of budgetary resources. With the enactment of the "Chief Financial Officers Act of 1990" (CFO Act) (Public Law 101-576), the "Government Management Reform Act of 1994" (GMRA) (Public Law 103-356) and subsequent accountability laws, the Congress called for the production of financial statements that fully disclose a federal entity's financial position and results of operations, and provide information not only for the effective allocation of resources, but also with which the Congress, agency managers, the public, and others can assess management performance and stewardship. Hence, the OMB, in consultation with the CFO Council, the President's Council on Integrity and Efficiency, and other interested parties, developed the formats and instructions for financial statements described and illustrated in this volume.

0103 POLICY

The provisions herein constitute guidance on the form and content of financial statements to be prepared implementing the SFFAS and the guidance issued by the OMB. These guidelines set out the reporting format and disclosure requirements for financial statements. Where, through additional disclosure, the value of a financial statement to its users is enhanced, that information also should be presented. This guidance is intended to provide a framework for financial statement preparation within which each DoD Component has the flexibility to develop

and include information useful both to its financial managers and program managers in making decisions. The hierarchy of accounting standards to be followed when recording accounting transactions is found in Volume 1, Chapter 8 of this Regulation.

0104 COVERAGE

A financial statement shall be prepared for each reporting entity identified in section 0106 of this chapter. This volume specifies the entities that shall be reported upon; identifies the level at which functions and or funds should be reported on a consolidated basis; notes the basis of accounting to be utilized; prescribes the specific authoritative guidance on financial statement format and disclosures that should be applied by personnel preparing the statements; and provides other instructions necessary for preparation of annual financial statements. These personnel may be in financial management or other disciplines (e.g., logistics or human resources).

★0105 EFFECTIVE DATE

The provisions of this volume are effective for the preparation of financial statements for fiscal years ending on and after September 30, 2000.

0106 DEPARTMENT OF DEFENSE REPORTING ENTITIES

★ 010601. Financial Statements Required by the OMB. The OMB requires the Department and most other major agencies to prepare Agency-wide financial statements in accordance with the GMRA (Public Law 103-356) covering all accounts and associated activities of each office, bureau, and activity of the agency. The DoD Agency-wide financial statements provide the financial status of the entire Department. In addition, there are eight Component reporting entities within the Department that, while included in the DoD Agency-wide statements, also are required by the OMB to prepare stand-alone audited financial statements. The appropriation and funds included in each of the annual financial statements are identified in Appendix A. The eight Component reporting entities are:

- A. The Department of the Army GF
- B. The Army WCF
- C. The Department of the Navy GF
- D. The Navy WCF
- E. The Department of the Air Force GF
- F. The Air Force WCF
- G. The Military Retirement Fund

H. The United States Army Corps of Engineers Civil Works

010602. Other Defense Organizations (ODO). In addition to the eight reporting entities identified in paragraph 010601, above, the remaining accounts of the Department are reported in two columns of the consolidating balance sheet for the DoD Agency-wide financial statements. The ODO-WCF column will include the financial activity of the WCF organizations that are not identified in paragraph 010601. The ODO-General Funds column will include the financial activity of the non-WCF organizations that are not identified in paragraph 010601.

010603. Consolidation of ODO Financial Statements. The consolidation of reporting entity financial statements for Treasury Index “97” funds, “ODO-General Funds,” shall follow the flow of funds from the apportionment of an appropriation, to allocation, suballocation, and allotment. The primary advantage of this consolidation method is that program managers and auditors can follow the flow of funds upward and downward and validate the receipt and execution of funds at all levels. For financial statement reporting, accounting activities shall consolidate allotment and suballotment information consistent with the flow (distribution) of funds. All principal staff assistant (PSA) offices for the Office of the Secretary of Defense and other organizations with Treasury Index Symbol “97” funds, identified in Table 2-3, shall receive a copy (hardcopy or computer file) of their combining financial statements. The consolidating/combining statements for each PSA/other organization identified shall include a column for each of its organization general funds and WCF subentities identified in Table 2-3. All Defense organization subentities identified in Table 2-3 also shall receive a copy (hardcopy or computer file) of the consolidating/combining financial statements which includes their financial information.

★ 010604. Internal Stand-alone DoD Annual Financial Statements. Although excluded from the formal list of DoD reporting entities required by the OMB to prepare financial statements and have those statements audited, the Department believes progress can be achieved if Defense Agencies prepare annual stand-alone financial statements and have those statements audited by certified public accounting (CPA) firms. In total, the Defense Agencies materially impact the Department’s agency-wide financial statements. Each Defense Agency identified in paragraph 010605 shall prepare financial statements and have them audited, beginning in FY 2000. Each Agency, with the advice of the Office of the Inspector General (OIG), DoD, shall establish an audit committee to oversee its financial audit. The purpose of the audit committee is to establish audit requirements, identify contract deliverables, and monitor the CPA firm’s execution of the contract. Each audit committee shall include a representative of the OIG, DoD.

★ 010605. The following Defense Agencies shall prepare internal stand-alone annual financial statements audited by CPA firms:

- A. Defense Logistics Agency
- B. Defense Finance and Accounting Service (DFAS)
- C. Defense Information Systems Agency

- D. Defense Contract Audit Agency
- E. Ballistic Missile Defense Organization
- F. Defense Advanced Research Projects Agency
- G. Defense Commissary Agency
- H. Defense Security Service
- I. Defense Threat Reduction Agency.

The internal stand-alone annual financial statements will include both GF and WCF, as applicable. These nine organizations will work with their supporting DFAS Center(s) to ensure the schedule presented in Chapter 2 of this volume is followed in a manner that will neither preclude meeting the individual milestones nor delay in any manner the reporting of the Department's audited financial statements required by the OMB.

- ★ 010606. List of Appropriation and Fund Symbols by Reporting Entity. Appendix A identifies the Appropriation and Fund Symbols that are included in the financial statements of each of the Department's eight Component and ODO reporting entities (all of which are included in the Department's Agency-wide financial statements).

0107 CONTENT OF AUDITED FINANCIAL STATEMENTS

- ★ 010701. The audited annual financial statements shall be comprised of eight major sections. Specific instructions for the preparation of the contents of each section are provided in individual chapters of this volume. The eight major sections and the sequence of their presentation are as follows:

- A. Overview of the Reporting Entity
- B. Principal Statements
- C. Notes to the Principal Statements
- D. Supporting Consolidating/Combining Statements
- E. Required Supplemental Stewardship Information
- F. Required Supplemental Information
- G. Other Accompanying Information
- H. Audit Opinion.

010702. Overview of the Reporting Entity. The Overview of the Reporting Entity is the first part of the annual financial statement. The Overview must provide readers with a clear and concise understanding of the reporting entity's activities, accomplishments, financial condition and results, problems and needs. It should tell the reader whether and how well the mission of the reporting entity is being accomplished and what, if anything, needs to be done to improve either program performance or financial performance. The overview includes a formal introductory transmittal letter from the head of the reporting entity. Guidance for the preparation of the Overview is provided in Chapter 3 of this volume.

★ 010703. Principal Statements and Notes to the Principal Statements. Principal statements and notes to the principal statements summarize financial information for individual funds and accounts within reporting entities and subentities. The amounts reported on the principal statements are based on specific general ledger account balances. General ledger crosswalks of accounts used to derive and report line item information for the principal statements are provided in Appendix C-H. Instructions for the preparation of the principal statements are contained in Chapters 4 through 9.

★ A. Principal Statements. The principal statements shall include:

1. Balance Sheet (Consolidated Comparative)
2. Statement of Net Cost (Consolidated Comparative)
3. Statement of Changes in Net Position (Consolidated Comparative)
4. Statement of Budgetary Resources (Combined Comparative)
5. Statement of Financing (Combined Comparative)
6. Statement of Custodial Activity (Comparative and required only for the agency-wide statements)

★ B. Notes to the Principal Statements. The notes to principal statements are an integral part of the financial statements and include a summarization of the accounting principles and methods of applying those principles that management has concluded are the most appropriate for presenting the entity's significant assets, liabilities, equity, revenues, expenses, and budgetary information. The notes also provide further detail of the amounts reported on the statements. In addition, when warranted, the notes identify departures from federal accounting standards or reporting requirements. In cases where individual line items of the financial statements cannot be obtained or a substitution is made from the requirements herein, the deficiencies shall be explained and the reason for noncompliance annotated in the footnotes. Where data used is known to be incomplete, deemed to be unreliable, or is an estimated (partially or full) amount, the note pertaining to the line(s) where such data is reported in the statement shall contain a reference to such data. The reference shall include the amount and explanation of

the circumstances regarding the availability and use of such data. The notes also contain disclosures required by the SFFASs. Instructions for the preparation of the required footnotes are contained in Chapter 10 of this volume.

010704. Required Supplementary Stewardship Information. Stewardship resources are investments by the federal government for the benefit of the Nation. The Required Supplementary Stewardship Information Section provides information on resources entrusted to federal agencies, highlights their long-term benefit nature, and demonstrates accountability over these resources. Specific guidance for reporting DoD stewardship assets is contained in Chapter 11 of this volume.

010705. Required Supplemental Information (RSI)

A. Statement of Budgetary Resources. Monitoring of budget execution is at the individual account level. Accordingly, budgetary information aggregated to the entity level of the Statement of Budgetary Resources should be disaggregated to the level of the entity's major account groupings and presented as supplementary information. Guidance for the preparation of this information is contained in Chapter 12 of this volume.

B. Deferred Maintenance. The Department is required to disclose in the RSI section of annual financial statements material amounts of deferred maintenance on property, plant, and equipment (PP&E). This reporting requirement is prescribed in the SFFAS No. 6, "Accounting for Property, Plant, and Equipment" and in the SFFAS No. 14, "Amendments to Deferred Maintenance Reporting." Guidance for the preparation of this information is contained in Chapter 12 of this volume.

C. Segment Information. Additional supplementary information is required for each franchise fund and other intragovernmental support revolving funds that are not separately reported on the entity's principal statements. Guidance for the preparation of this information is contained in Chapter 12 of this volume.

010706. Other Accompanying Information. The other accompanying information section of the DoD financial statements shall contain the information identified in Table 1-1, section 10 and any other information that the entity management wishes to provide. Also see Chapter 3, section 0304 of this volume.

★ 010707. Financial Statement Organization. The financial statements should be organized as shown in Table 1-1 as follows:

DETAILED OUTLINE OF DOD ANNUAL FINANCIAL STATEMENTS

Section Sequence	Major Components of Annual Financial Statements (Hard copy and files for Internet)	DoD Entity Reports	DoD Agency-Wide
1	Cover	Required	Required
2	Table of Contents	Required	Required
3	Message(s) from the Secretary of the Military Department; Chief, U.S. Army Corps of Engineers; or the Director of a Defense Agency as applicable for the reporting entity.	Required	Required
4	Overview	Required	Required
5	Principal Statements		
★5.1	Balance Sheet, Consolidated Comparative	Required	Required
★5.2	Statement of Net Cost, Consolidated Comparative	Required	Required
★5.3	Statement of Changes in Net Position, Consolidated Comparative	Required	Required
★5.4	Statement of Budgetary Resources, Combined Comparative	Required	Required
★5.5	Statement of Financing Combined Comparative	Required	Required
★5.6	Statement of Custodial Activity, Consolidated Comparative	Not Applicable	Required
6	Notes to Principal Statements	Required	Required
7	Supporting Consolidating/Combining Statements		
7.1	Balance Sheet, Consolidating	Required ¹	Required
7.2	Statement of Net Cost, Consolidating	Required ¹	Required
7.3	Statement of Changes in Net Position, Consolidating	Required ¹	Required
7.4	Statement of Budgetary Resources, Combining (By subentity)	Required ¹	Required
7.5	Statement of Financing, Combining	Not Required	Required
8	Required Supplementary Stewardship Information		
8.1	National Defense PP&E	Required ¹	Required
8.2	Stewardship Land	Required ¹	Required
8.3	Heritage Assets	Required ¹	Required
8.4	Non-Federal Physical Property	Required ¹	Required
8.5	Research and Development	Required ¹	Required
9	Required Supplementary Information		
★9.1	Disaggregated Statement of Budgetary Resources, Combining (By appropriation group, see Appendix A)	Required ¹	Required

Table 1-1

Section Sequence	Major Components of Annual Financial Statements (Hard copy and files for Internet)	DoD Entity Reports	DoD Agency-Wide
9.2	Deferred Maintenance	As Applicable	Required
9.3	Segment Information (See Chapter 12, section 1202)	As Applicable	Required
9.4	Intragovernmental Amounts	Required	Required
10	Other Accompanying Information (See Chapter 3, section 0304)		
10.1	Any Additional Performance Information Not Provided in the Overview	As Applicable	As Applicable
10.2	Detailed List of Appropriations, Funds, and Accounts Included in Financial Statements	Required	Required
10.3	Reporting of Foreign Military Sales Activity (See Chapter 2, paragraph 020104)	Not Applicable	Required
10.4	Other Information Which the Entity Management Wishes to Provide	As Applicable	As Applicable
11	Audit Opinion(s)		
11.1	Inspector General, DoD Audit Opinion or Endorsement	Required	Required
11.2	Audit Opinion of the U.S. Army Audit Agency, Naval Audit Service, Air Force Audit Agency or CPA Firm (e.g., for the Military Retirement Trust Fund)	Required	Not Applicable
Footnotes:			
1. Not Applicable to the Military Retirement Fund.			

Table 1-1 (Continued)

★0108 FINANCIAL STATEMENT AUDITS

★ 010801. DoD Reporting Entity Audits. The OIG, DoD shall render an audit opinion on the DoD Agency-wide financial statements. The OIG, DoD opinion shall be based, in part, on the opinions issued by the Military Department audit agencies or CPA firms for each of the reporting entities identified in paragraph 010601, above. In addition, the OIG, DoD shall provide an endorsement to the audit opinion for each of the reporting entity financial statements opined on by the applicable Service Audit Agency or CPA audit firm.

★ 010802. Other Defense Organizations Audits. While the OIG, DoD will not issue separate audit opinions on the financial statements of the ODO included in the DoD Agency-wide financial report, the financial statements and records of the organizations shall be included in the audits performed to support the opinion issued by the OIG, DoD on the DoD Agency-wide financial statements.